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No. 03-1407

IN THE
SUPREME COURT OF THE UNITED STATES

RICHARD GERALD ROUSEY and BETTY JO ROUSEY,
Petitioners,

v.

JILL R. JACOWAY,
Respondent.

On a Writ of Certiorari to the United States
Court of Appeals for the Eighth Circuit

BRIEF OF AARP AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

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QUESTIONS PRESENTED

1. Whether a debtor's right to receive payments from the debtor's own Individual Retirement Account (IRA), complying with the Internal Revenue Code (I.R.C.) § 408, qualifies as "exempt property" under 11 U.S.C. § 522(d)(10)(E) of the Bankruptcy Code.

2. Whether the exemption under 11 U.S.C. § 522(d)(10)(E) includes a debtor's right to receive future payments from a qualified IRA where the debtor is neither receiving – nor is yet eligible to receive – payments in accordance with the Internal Revenue Code.

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INTEREST OF AMICUS CURIAE[1]

In the last year, more than 1.6 million Americans made the difficult and painful decision to file for personal bankruptcy. Americans age 65 and older are now the fastest growing group in bankruptcy.

AARP is a nonpartisan, nonprofit membership organization of more than 35 million people age 50 or older, working and retired, that is dedicated to addressing the needs and interests of older Americans. As *amicus*, it periodically has provided the Supreme Court with the perspective of its members. Last year, for example, AARP submitted an *amicus* brief in *Till v. SCS Credit Corp.*, 124 S. Ct. 1951 (2004), a decision that established the appropriate rate of interest on secured debt in Chapter 13.

Almost half of AARP's members work, and many contribute to a variety of retirement savings plans, including Individual Retirement Accounts (IRAs). Increasingly, older Americans, often with decades of work experience, find themselves unable to avoid financial devastation from job layoffs, catastrophic illness, loss of a spouse, or downturns in the nation's economy. After exhausting other options, many turn to the bankruptcy system to try to save their homes, to obtain limited relief from creditors, and to protect retirement

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[1] Each party's written consent for the submission of AARP's brief *amicus curiae* is on file with the Clerk of the Court. Pursuant to SUP. CT. R. 37.6, AARP states that no counsel for any party authored this brief in whole or in part and that no party or entity other than AARP, its affiliates, or counsel made a monetary contribution to the preparation or submission of this brief.

savings they have spent years accumulating. The financial well-being of older Americans, secure in the knowledge that their retirement savings are protected even if bankruptcy becomes inescapable, is of substantial importance to AARP and its members.

This case is about the meaning of a single provision of the federal bankruptcy law. But the significance of this case, particularly for older Americans, lies not in the rules of statutory construction but with the desire of Congress to encourage and protect the retirement savings of all Americans. Are IRAs protected by statute, available, especially in retirement, to facilitate a debtor's self-support and keep the promise of 100 years of bankruptcy law? Or are they indistinguishable from fine jewelry or ordinary bank accounts that can be used to satisfy creditors?

Like the U.S. Courts of Appeal, the parties disagree on whether IRAs qualify for the exemption in 11 U.S.C. § 522(d)(10)(E). The U.S. Courts of Appeal have reached different judgments about what Congress intended. As a result, this is also a case about the purposes of the exemption in § 522(d)(10)(E) and the complementary goal of Congress in encouraging and facilitating retirement savings through the tax code.

Richard and Betty Jo Rousey filed for bankruptcy in 2001. Jill Jacoway, the Chapter 7 bankruptcy trustee for their case, objected to the Rouseys' claimed exemptions. The Rouseys established two IRAs with retirement funds "rolled over" from pension plans with their former employer. In deciding their case, this Court will consider whether the Rouseys' ability, consistent with the Internal Revenue Code, to withdraw money from these IRAs upon payment of a ten

percent penalty makes their IRAs – and the IRAs of millions of other Americans – ineligible for the exemption. If the Court concludes that some or all IRAs are subject to the claims of creditors as if they were ordinary bank accounts, it will consider the related question of whether the exemption in § 522(d)(10)(E) is available only to those presently withdrawing – or with the present right to withdraw – funds from their IRAs without penalty.

Section 522(d)(10)(E) exempts from the reach of creditors a debtor's "right to receive" any payments under a "stock bonus, pension, profitsharing, annuity, or similar plan or contract . . . to the extent reasonably necessary for the support of the debtor and any dependent of the debtor." In short, it exempts income earned and saved but not yet paid.

IRAs are a critical source of retirement savings for the self-employed, workers without employer-sponsored retirement plans, and those who have rolled over distributions of plan benefits from former employers. Although IRA savings are modest for most Americans – the median IRA in 2003 held $30,000 for households with traditional IRAs only – they represent particularly important safeguards for individuals with no other retirement savings.

Under the decision of the U.S. Court of Appeals for the Eighth Circuit, all of these savings would be lost in bankruptcy. Under the interpretation mandated in the U.S. Court of Appeals for the Third Circuit, anyone under the age of 59½ would lose these savings. Neither is correct.

Older Americans who lose their IRAs in bankruptcy will have a sharply reduced ability to support themselves in their retirement years. Rebuilding retirement savings is a

daunting task for anyone, and it is particularly difficult for older Americans emerging from bankruptcy. Many older Americans have health issues that severely limit their ability to work. Those able to work often find that they need retraining to re-enter the workforce after years of initial retirement. Finding a job as an older American can be a difficult and disheartening undertaking. Even with statutory protection, age discrimination continues to be an obstacle. Older workers, even those with years of white-collar work experience, are likely to find only low wage jobs with significant reductions in pay. Basic living expenses consume their modest wages, leaving little, if anything, for savings.

Social Security is the major income source for two out of three older Americans and has been instrumental in lifting millions out of poverty. Yet these benefits are limited. For older Americans facing increasing medical and housing-related expenses, even modest savings make a substantial difference in retirement. Under the decisions at issue in this case, older Americans who have counted on IRAs for their retirement and who need to file for bankruptcy will lose even this modest measure of security.

Congress has made a deliberate decision to protect the ability of Americans to support themselves even after a severe personal economic reversal. It also has decided to encourage self-support in retirement by providing protection to retirement savings through both the tax code and the bankruptcy law. This protection has heightened importance for older Americans. It is not an academic or theoretical question. For thousands of older Americans, it is a matter of financial survival.

STATUTE AT ISSUE

11 U.S.C. § 522

(d) The following property may be exempted under subsection (b)(1) of this section:

* * * *

(10) The debtor's right to receive—

(A) a social security benefit, unemployment compensation, or a local public assistance benefit;

(B) a veterans' benefit;

(C) a disability, illness, or unemployment benefit;

(D) alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;

(E) a payment under a stock bonus, pension, profitsharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor, unless—

(i) such plan or contract was established by or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose;

(ii) such payment is on account of age or length of service; and

(iii) such plan or contract does not qualify under section 401(a), 403(a), 403(b), or 408 of the Internal Revenue Code of 1986.

STATEMENT OF THE CASE

The Bankruptcy Reform Act of 1978 modernized federal bankruptcy law. *See* S. Rep. No. 95-989 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787. The result of nearly a decade of work, the Act changed both the substantive and procedural law of bankruptcy. *United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 240 (1989). The law in § 522 established a set of federal exemptions that "permit an individual debtor to take out of the estate property that is necessary for a fresh start and for the support of himself and his dependents." H. Rep. No. 95-595, at 176 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6136; *see United States v. Security Industrial Bank*, 459 U.S. 70, 83 (1982) (Blackmun, J., dissenting). This case involves the scope of one portion of one exemption, 11 U.S.C. § 522(d)(10)(E), "the debtor's right to receive" payments from individual retirement accounts.

Richard and Betty Jo Rousey voluntarily filed a joint bankruptcy petition under Chapter 7 in April 2001. The Rouseys' assets included two IRAs valued at $42,915.32 and $12,118.16 in deposit accounts holding funds rolled over from their previous employer's pension plans approximately two years earlier. The Rouseys elected to use the federal exemptions in 11 U.S.C. § 522.[2] They claimed exemptions

[2] In states like Arkansas, where the Rouseys live, that have not opted out of the federal exemption system, debtors can choose either the exemptions in § 522(d) or the exemptions available under applicable state and nonbankruptcy federal law. Approximately 34 states have opted out the federal exemption system. 4 COLLIER ON BANKRUPTCY ¶ 522.01, at 522-11 (15th ed. rev. 2004). Some of the states that have opted out of the federal exemption plan use language that parallels § 522(d) in their state exemption law. *See id.*; *see, e.g., In re Huebner*, 986 F.2d

for their IRAs in the amount of $10,681 ($5,033 and $5,648, respectively, for the two IRAs) pursuant to § 522(d)(5), not at issue here, and exemptions for the remaining IRA amount of $44,352.48 ($37,882.32 and $6,470.16, respectively) pursuant to § 522(d)(10)(E). The bankruptcy trustee objected to the (d)(10)(E) exemptions but not to the (d)(5) exemptions.[3]

The principal question in this case is: Whether a debtor's right to receive payment from an IRA that qualifies under I.R.C. § 408 qualifies as "exempt property" under 11 U.S.C. § 522(d)(10)(E) of the Bankruptcy Code. The bankruptcy court found that the IRAs were not exempt under § 522(d)(10)(E), and the bankruptcy appellate panel affirmed. The Eighth Circuit ultimately affirmed the trustee's objection as well, although on narrower grounds than the lower courts had used.

A second question in this case arises only if the Court rules against the Rouseys on the first question: Whether the exemption for IRAs under 11 U.S.C. § 522(d)(10)(E) is available only where a debtor is receiving – or is eligible to

1222, 1224 (8th Cir. 1993) (Iowa statute); *In re Dubroff*, 119 F.3d 75, 78 (2nd Cir. 1997) (New York statute); *In re McKown*, 203 F.3d 1188, 1189 (9th Cir. 2000) (California law). Others expressly exempt IRAs. *See* 4 COLLIER ON BANKRUPTCY ¶ 522.09[10][b], at 522-64; *see, e.g., In re Yuhas*, 104 F.3d 612, 613 (3rd Cir. 1997) (New Jersey law); *In re Meehan*, 102 F.3d 1209, 1211 (11th Cir. 1997) (Georgia law).

[3] Section 522(d)(5) allows a debtor to exempt his "aggregate interest in any property, not to exceed in value $925 plus up to $8,725 of any unused amount of the exemption" under subsection (d)(1) for the debtor's residence or burial plot.

receive – payments in accordance with the Internal Revenue Code.[4] Courts in the U.S. Court of Appeals for the Third Circuit allow IRAs the exemption only where the debtor is at least age 59½ and, accordingly, statutorily eligible to receive payments from the IRA without penalty. This interpretation is based on a 1983 appellate decision in which the court found no basis in § 522(d) for Congressional concern for the debtor's long-term security. *See In re Clark*, 711 F.2d 21 (3rd Cir. 1983).

Four other Courts of Appeal have considered whether IRAs similar to the Rouseys' IRAs qualify for the exemption either under § 522(d)(10) or parallel state statutes. *See In re Carmichael*, 100 F.3d 375 (5th Cir. 1996); *In re Dubroff*, 119 F.3d 75 (2nd Cir. 1997); *In re McKown*, 203 F.3d 1188 (9th Cir. 2000); *In re Brucher*, 243 F.3d 242 (6th Cir. 2001). All four concluded that IRAs are eligible for the exemption. *See also* Pet. at 8 n.6 (listing bankruptcy courts in agreement). One appellate court also asked whether § 522(d)(10)(E) is limited to present payments and present rights to payments, concluding that the provision also protects the right to receive future payments even where no right to present payments exists. *See Carmichael*, 100 F.3d at 379.

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[4] This Court granted *certiorari* on the following question: "Should this Court grant *certiorari* to resolve the three way circuit conflict over whether and to what extent Individual Retirement Accounts (IRAs) are exempt from a bankruptcy estate under 11 U.S.C. § 522(d)(10)(E)." Therefore, this second question was in effect included in the petition, and it should be considered by the Court. *See* SUP. CT. R. 14.1(a).

SUMMARY OF THE ARGUMENT

The economic vulnerability of older Americans is a growing national tragedy. The rate of bankruptcy filings, which remains at record levels, is rising faster among those 55 and older than the general population. The rate of increase in filings is greatest among those 65 and older.

The practical consequences of the Court's decision will be significant as increasing numbers of Americans approaching retirement are faced, for the first time, with economic circumstances that leave them little choice but to file for bankruptcy. For the self-employed and millions of others without employer-sponsored retirement plans, often small business employees, IRAs are one of the few available retirement savings plans.

Under the Eighth Circuit's decision, the only IRAs that qualify for the exemption are those that limit withdrawals exclusively to circumstances of illness, disability, death, fixed age, or length of service. Yet the record contains no evidence of IRAs that do not permit withdrawals only in those circumstances. Because no IRAs meet the standard imposed by the Eighth Circuit, even modest retirement savings are lost in bankruptcy. For individuals in, or approaching, retirement – relying on IRAs as their principal or only source of retirement savings – the consequences of such a loss will be severe, particularly for those with limited work opportunities or health constraints.

The interpretation of § 522(d)(10)(E) used in the Third Circuit also has devastating consequences for debtors with IRAs. Under that rule, only individuals entitled to "present payments" from IRAs – that is, persons who already have

reached the age of 59½ and are entitled by statute to funds from their IRAs – may exempt IRA funds. Debtors 59½ or younger lose their IRAs in bankruptcy.

Both of these judicial interpretations erroneously read into § 522(d)(10)(E) limitations not present in the text of the statute. Nowhere does the statute limit the exemption to contracts or plans for which payments are made "only" on account of illness, disability, age, or length of service. And nothing in the exemption's language requires the present receipt of payments. To the contrary, Congress has authorized exemptions for the "right to receive" payments, leaving them available for individuals and families to support themselves after bankruptcy. The interpretations of the Eighth and Third Circuits collide with the provision's text, the statutory framework and Congressional intent.

ARGUMENT

Since Congress enacted the modern Bankruptcy Code in 1978, this Court has decided a litany of statutory construction cases, culminating in two decisions in just the last term.[5] In bankruptcy, like all cases involving statutory

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[5] *See, e.g., Security Industrial Bank*, 459 U.S. 70 (the effect of 11 U.S.C. § 522(f)(2) on certain types of property liens); *Ron Pair*, 489 U.S. 235 (whether 11 U.S.C. § 506(b) entitles some creditors to receive postpetition interest); *Grogan v. Garner*, 498 U.S. 279 (1991) (evidentiary standard for exceptions in 11 U.S.C. § 523(a)); *Patterson v. Shumate*, 504 U.S. 753 (1992) (meaning of "nonbankruptcy law" in 11 U.S.C. § 541 (c)(2)); *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994) (meaning of "reasonably equivalent value" in 11 U.S.C. § 548(a)(2)); *Bank of America Nat'l Trust & Sav. Ass'n v. 203 LaSalle St. P'ship*, 526 U.S. 434 (1999) (effect of 11 U.S.C. § 1129(b)(2)(B)(ii) on participation by old equity holders in "new value" transactions); *Lamie v. United*

interpretation, "[t]he starting point in discerning congressional intent is the existing statutory text." *Lamie v. United States Trustee*, 124 S. Ct. 1023, 1030 (2004). "'[W]hen the statute's language is plain, the sole function of the courts – at least where the disposition required by the text is not absurd – is to enforce it according to its terms.'" *Id.* (*quoting Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 (2000) (internal citations omitted)).

The text of the statute here is plain and dispositive. Although the terms "IRA" or "Individual Retirement Account" do not appear in § 522(d)(10)(E), an IRA is a "plan or contract" providing for payments "on account of . . . age" that is "similar" to the plans and contracts specifically named in the provision. Subsection (iii) includes a reference to I.R.C. § 408, the section that sets forth requirements for IRAs to qualify for certain tax benefits, and it reinforces that plain language. Subsection (iii) denies the exemption to any "plan or contract" that "does not qualify" under I.R.C. § 408. *See* 11 U.S.C. § 522(d)(10)(E)(i)-(iii). There would be no need for this important reference to § 408 if IRAs were not covered by the exemption in the first place. IRAs in general and the Rouseys' IRAs specifically qualify under § 408.

The context of § 522 is equally compelling. The statute "exempt[s]" from property of the estate a limited amount of cash, other assets, rights and interests, leaving them in the hands of the debtor to begin a post-bankruptcy economic

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States Trustee, 124 S. Ct. 1023 (2004) (whether 11 U.S.C. § 330(a)(1) authorizes compensation to debtors' attorneys from estate funds); *Till*, 124 S. Ct. 1951 (appropriate rate of interest under 11 U.S.C. § 1325(a)(5)(B)(ii) due certain creditors).

life. Some exemptions, like "professional books" and the "tools of the [debtor's] trade," are specifically intended to preserve the debtor's ability to earn or receive income in the future. So are the specific exemptions for Social Security, unemployment, disability, and other benefits in § 522(d)(10)(A)-(D).

Congress was acutely aware that a bankruptcy law that left a debtor stripped bare, unable to earn a living, would not advance one of the principal goals of the Code: to ensure that debtors could quickly become not only technically solvent but self-supporting.[6] Without that, individuals and families emerging from bankruptcy would be forced to depend on charity or the government. By protecting retirement accounts, no less than tools of the trade and Social Security payments, Congress has advanced that same goal: making it easier for older Americans to support themselves when their prime earning years have passed.

Congress has clearly expressed its intent to facilitate, to encourage and to protect retirement savings, whether they are in IRAs or another recognized plan. It has done that by providing favorable tax treatment for retirement savings. When the language of the Bankruptcy Code is so clear, especially with its explicit reference to the Internal Revenue Code, no court should be tempted to take away the benefits

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[6] The importance of exemptions in personal bankruptcy is a concept at least as old as the United States itself: "Only non-exempt property could be taken in execution, which in most colonies and states meant that some, usually small, portion of clothing, bedding, necessary household items, farm implements, and tools of a trade were shielded from seizure." Bruce H. Mann, *Republic of Debtors: Bankruptcy in the Age of American Independence* 30 (2002).

that Congress has provided, especially for individuals and families trying to support themselves after bankruptcy.

I. A DEBTOR'S RIGHT TO RECEIVE PAYMENT FROM AN IRA THAT COMPLIES WITH THE INTERNAL REVENUE CODE SHOULD AUTOMATICALLY QUALIFY AS "EXEMPT PROPERTY."

Section 522(d)(10)(E) authorizes a debtor to exempt from the bankruptcy estate the debtor's "right to receive . . . a payment under a stock bonus, pension, profitsharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service . . . ."[7] 11 U.S.C. § 522(d)(10)(E). The same section *excludes* from the exemption a plan or contract which: "(i) . . . was established by or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose; (ii) such payment is on account of age or length of service; *and* (iii) such plan or contract does *not* qualify under section 401(a), 403(a), 403(b), or 408 of the Internal Revenue Code of 1986." 11 U.S.C. § 522(d)(10)(E) (emphasis added). IRAs that meet the requirements of I.R.C.

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[7] This exemption is limited to amounts "reasonably necessary for the support of the debtor and any dependent of the debtor . . . ." The Eighth Circuit did not address this provision, and it is not at issue here. However, the "reasonably necessary" requirement reinforces the exemption's compatibility with the purposes of the consumer bankruptcy statute. The limitation prevents the use of an IRA "or similar plan or contract" as a shelter to defraud creditors. Yet, limited to the funds reasonably necessary for a family's support, the exemption makes self-sufficiency and economic recovery possible.

§ 408 qualify for the exemption. The Rouseys' IRAs meet those requirements. Most IRAs do.

A. The Plain Language Of § 522(d)(10)(E)(iii) Should Leave No Doubt That IRAs, As "Similar Plans Or Contracts," Qualify For The Exemption.

The application of § 522(d)(10)(E)(iii) properly "begins where all such inquires must begin: with the language of the statute itself." *Ron Pair*, 489 U.S. at 241 (*citing Landreth Timber Co. v. Landreth*, 471 U.S. 681, 685 (1985)). And this is also where the inquiry should end. *Id.*

The explicit reference to I.R.C. § 408 in § 522(d)(10)(E)(iii) is dispositive. An IRA that does not qualify under the Internal Revenue Code does not qualify for the exemption. Accordingly, a qualifying IRA should trigger the exemption as long as it is "similar" to a "stock bonus, pension, profitsharing, [or] annuity" plan. An IRA that meets Internal Revenue Code requirements – which include provisions for penalty-free payments based on age, death, or disability, *see* I.R.C. §§ 408(d), 72(t) – falls squarely within the exemption's scope. Far from excluding IRAs from the exemption, Congress at the very least made them eligible for the exemption.

Congress used the term "plan or contract" in both the exemption and in its limiting provision, subsection (iii). The only logical reading of section 522(d)(10)(E) is that an IRA that qualifies by reference under I.R.C. § 408 is a "similar plan or contract" under the exemption. *See Sorenson v. Secretary of Treasury*, 475 U.S. 851, 860 (1986) ("The normal rule of statutory construction assumes that 'identical

words used in different parts of the same act are intended to have the same meaning'") (*quoting Helvering v. Stockholms Enskilda Bank*, 293 U.S. 84, 87 (1934)) (internal citations omitted).[8] Section 522(d)(10)(E)(iii) limits the exemption. There would be no need for the reference to § 408, requiring compliance to qualify for the exemption, if IRAs had already been excluded from the provision and were, therefore, not covered by the exemption in the first place.

Each word in a statute has meaning. *See Dunn v. CFTC*, 519 U.S. 465, 472 (1997) ("Our reading of the exemption is therefore also consonant with the doctrine that legislative enactments should not be construed to render their provisions mere surplusage"); *see also* 2A Norman J. Singer, Statutes and Statutory Construction § 46:06 (6th ed. 2000). By contrast, the Eighth Circuit's decision renders meaningless the reference to § 408 in subparagraph (iii).

If IRAs can never be exempted under § 522, there would be no qualified and, therefore, exempt § 408 plans or contracts to distinguish from non-qualified and, therefore, non-exempt plans. The reference to § 408 in subparagraph (iii) would be "mere surplusage." Unlike the provision at issue in *Lamie*, 124 S. Ct. at 1031, treating the reference to § 408 as surplusage here would create – rather than resolve – ambiguity. Nor is there any evidence that the reference to §

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[8] *See also Commissioner v. Lundy*, 516 U.S. 235, 249-250 (1996) ("[W]e have been given no reason to believe that Congress meant the term 'claim' to mean one thing in [11 U.S.C.] § 6511 but to mean something else altogether in the very next section of the statute"); *Bank of America*, 526 U.S. at 451 ("[A] given phrase is meant to carry a given concept in a single statute").

408 is a drafting error. *Cf. Chickasaw Nation v. United States*, 534 U.S. 84, 89 (2001). Accordingly, there is no basis to depart from the well-established principle that a statute should not be construed to render any of its words surplusage.

B. IRAs Are Sufficiently Similar To The Four Types Of Plans Or Contracts Listed In § 522(d)(10)(E) To Qualify As Exempt.

Congress enacted § 522 "to permit an individual debtor to take out of the estate that property which is necessary for a fresh start and for the support of himself and his dependents." H. Rep. No. 95-595, at 176, *reprinted in* 1978 U.S.C.C.A.N. at 6136. The provisions of § 522(d)(10) "exempt[] certain benefits that are akin to future earnings of the debtor." H. Rep. No. 95-595, at 362, *reprinted in* 1978 U.S.C.C.A.N. at 6318. The four types of contracts or plans expressly named in subparagraph (d)(10)(E) as *per se* exempt are substitutes for future earnings. IRAs serve the same purpose.

Even were the text of § 522(d)(10)(D) otherwise ambiguous on the scope of the IRA exemption, the Rouseys' IRA – and IRAs generally – are plans or contracts "similar" to stock bonus, pension, profitsharing, and annuity plans or contracts from which payments are made on account of illness, disability, death, age, or length of service. While § 522 obviously does not use the term "IRA" or "individual retirement account," it uses the phrase "similar plan or contract" to expand the reach of the exemption. The purpose of both § 522 and I.R.C. § 408, the provision authorizing IRAs, demonstrates that IRAs are "similar" plans or

contracts. The Eighth Circuit appears to concede as much. *See* Pet. App. at 5a.

Congress first authorized IRAs in 1974. These first IRAs extended some of the tax benefits of employer pension plans to those whose employers did not have such plans. The statute authorized a deduction for up to 20 percent of earned income, not to exceed $1,500, "for retirement savings." H. Conf. Rep. No. 93-1280 (1974), *reprinted in* 1974 U.S.C.C.A.N. 5038, 5115; *see id., reprinted in* 1974 U.S.C.C.A.N. at 5122 (proceeds of IRAs "are to constitute retirement income for purposes of the retirement income credit"). The statute also authorized tax-free rollovers into IRAs to facilitate pension portability and transfers. *See id., reprinted in* 1974 U.S.C.C.A.N. at 5121-22; *see generally* H. Rep. No. 93-807 (1974), *reprinted in* 1974 U.S.C.C.A.N. 4670, 4671; S. Rep. No. 93-383 (1974), *reprinted in* 1974 U.S.C.C.A.N. 4890, 4898.

Congress made IRAs universally available in 1981 as a general incentive to save for retirement and increased the contribution amounts eligible for a tax deduction. *See* S. Rep. No. 97-144, at 112 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 214 ("The Committee is concerned that the resources available to individuals who retire are often not adequate to avoid a substantial decrease from preretirement living standards. . . . [R]etirement savings by individuals can make an important contribution . . . [and] the present level of individual savings is too often inadequate for this purpose"); *id.* at 215 (The bill "is designed to promote greater retirement security").

Congress also has made the IRA the investment vehicle for simplified employee pensions, *see* I.R.C. § 408(k), and

for simple retirement accounts, *see* I.R.C. § 408(p) – that is, retirement plans specifically designed to provide employees of small employers access to retirement alternatives similar to those available to employees of larger employers. In 2001, Congress authorized transfers of funds from IRAs to qualified plans, such as 401(k) plans, *see* I.R.C. § 408(d)(3), a further example of the Congressional efforts to facilitate portability and encourage retirement savings. Through these and other provisions of § 408, Congress has created substantial incentives for the use of IRAs.

The incentives have worked. More than 45 million taxpayers have IRAs. According to a recent Congressional Research Service Report, IRA savings have grown steadily from $85 billion in 1983 to $2.5 trillion at the end of 2001. *See* Paul J. Graney, *Individual Retirement Accounts: A Fact Sheet, CRS Report for Congress*, Code 94-83 EPW (Dec. 5, 2003). New contributions, however, have not been the main source of this growth. While new contributions accounted for 81 percent of the growth in IRA assets in 1984, they accounted for only about two percent of growth in the late 1990s. A key reason for this shift has been the steady stream of asset rollovers from employer pension plans to IRAs. *Id.*

The Rouseys established their IRAs the same way many older workers did; they used funds rolled over from their Northrop Grumman plans maintained by their former employer. Pet. App. at 2a, 8a.[9] Indeed, older workers have

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[9] As one of the judges on the Bankruptcy Appellate Panel that heard the Rouseys' appeal acknowledged, their "pensions would have been exempt had they filed their bankruptcy petition while employed by Northrop Grumman." Pet. App. at 18a.

more IRA plans than any other age group because the bulk of IRA assets are rolled over from previous pensions. *See* Jules H. Lichtenstein and Satyendra Verma, *Older Workers' Pension Plan and IRA Coverage*, at 3 (Oct. 2003), at http://research.aarp.org/econ/dd91_retire.pdf, and *Retirement Plan Coverage of Baby Boomers & Retired Workers: Analysis of 1998 SIPP Data*, at 13-14 (July 2003), at http://research.aarp.org/econ/ 2003_10_98sipp.pdf.

For the Rouseys and millions of other older Americans, the IRA became an indispensable part of retirement planning. More than four million Americans aged 53-64 – that is, almost 25 percent of that age group – maintain an IRA at least partially funded from an employer pension plan. Lichtenstein and Verma, *1998 SIPP Data*, at 14. IRAs are also a key component of retirement planning for the more than two million Americans aged 53-64 who have never had a pension plan. *See id.*

An IRS study of tax year 2000 returns emphasizes the importance of IRAs in the retirement planning of older Americans. It found that 39 percent of taxpayers aged 50-60 have IRAs, and the average value of these IRAs was $64,701. Peter J. Sailer and Sarah E. Nutter, *Accumulation and Distribution of Individual Retirement Arrangements, 2000*, at 126, 134 (Spring 2004), at http://www.irs.gov/pub/irs-soi/00retire.pdf. More recent data reinforce the importance of IRAs, particularly for older Americans. The median age of heads of households with traditional IRAs was 52. *See* Investment Company Institute, *IRA Ownership in 2003*, Fundamentals, Sept. 2003, at http://www.ici.org/stats/res/fm-v12n3.pdf. The median assets held in IRAs totaled $30,000 for households with traditional IRAs and $20,000 for households with any type of IRA. *Id.*

IRA payments that meet the requirements of § 408 are functionally the same as a stock bonus, pension, profitsharing, and annuity plan or contract. They are the functional equivalent as well of the Social Security, unemployment, and disability payments exempted under the statute. Congress repeatedly has expressed its concern for the retirement security of Americans. To that end, it has created specific benefits and savings incentives for self-employed individuals, individuals without employer-based pension plans, and those like the Rouseys who, consistent with § 408, rolled funds from pension and other exempt funds into IRAs when those plans terminated or employment ended.

Congress has utilized the IRA "to serve as a sort of universal conductor through which transfers must pass if they are to avoid the rocks and shoals of inadvertent taxable events." *Carmichael*, 100 F.3d at 378. Section 522 cannot be read, literally or logically, to exclude IRAs that qualify under § 408. IRAs should remain a recognized and valuable vehicle for retirement savings, not a trap for honest taxpayers who utilize § 408 for pension rollovers and other fund transfers intended for retirement only to lose them in bankruptcy.

C. The Exemption In § 522(d)(10)(E) Is Not Limited To Plans Or Contracts That Permit Payments Only Based On Illness, Disability, Death, Age, Or Length Of Service.

Both the text and purpose of § 522(d)(10)(E) demonstrate that IRAs that qualify under § 408 also should qualify for the exemption. Yet, under the Eighth Circuit's interpretation, the Rouseys' IRAs do not qualify because

they permit withdrawals prior to age 59½ if a ten percent penalty is paid. This conclusion categorically excludes IRAs from the exemption along with a number of stock bonus, pension, profitsharing, and annuity plans and contracts because at least some permit withdrawals prior to age 59½ with a ten percent penalty. *See* I.R.C. § 72. Whether this limitation applies only to IRAs, or to all "similar" plans or contracts, the result is contrary to both the text and purpose of § 522.

IRA holders may make early withdrawals subject to a tax penalty. That is not, however, a statutory basis for denying the bankruptcy exemption's protection to IRAs. By tax law, "the right to receive payments" from an IRA without penalty can be triggered by four events: reaching age 59½, death, disability or medical care. *See* I.R.C. §§ 408, 72(t). These four events mirror the first four of the five triggering events in the bankruptcy exemption (excluding "length of service").

To qualify for the exemption, the statute requires that the plan or contract give the debtor a right to receive payments on account of illness, disability, death, age, *or* length of service. The statute does not require that any – or all – of the tests be the strict or exclusive method of triggering a repayment, only that repayment can be triggered by at least one of these events. The only limitations imposed by the Bankruptcy Code apply to plans that are not qualified under the enumerated IRA provision. The Rouseys' IRAs qualify under § 408 and thus meet the standard set forth in the Bankruptcy Code.

In concluding otherwise, the Eighth Circuit ignored the plain language of the bankruptcy statute. The appellate court impermissibly read into the statute a requirement that the

right to receive payment be conditioned solely on one of the events listed in § 522(d)(10)(E) – a limitation that does not appear in the text.

The bankruptcy court below acknowledged that few, if any, IRAs could meet this requirement. *See* Pet. App. 33a n.5. The lower court's suggestion that IRAs somehow "could" comply with the Eighth Circuit's standard by including a spendthrift provision[10] illustrates the flawed logic of its interpretation. If an IRA had a valid spendthrift provision, the IRA would be excluded from the estate entirely under 11 U.S.C. § 541(c)(2). *See* 4 COLLIER ON BANKRUPTCY ¶ 522.09[10][b], at 522-62; *see also Patterson*, 504 U.S. at 762 ("§ 522(d)(10)(E) exempts from the bankruptcy estate a much broader category of interests than § 541(c)(2) excludes").[11] Under the Eighth Circuit's reading,

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[10] "Spendthrift trusts" are authorized in most states. In Arkansas, for example, they include "[a]ny retirement plan which meets the requirements of § 401 or § 403 of the Internal Revenue Code of 1986, as amended, which contains a prohibition against alienation[,] and a prohibition against attachment shall be conclusively presumed for the purposes of Arkansas law to be a spendthrift trust." Ark. Code § 28-69-501 (2003). A spendthrift trust can only be created in Arkansas by an express restraint on alienation. *See Sanders v. Putman*, 866 S.W.2d 827, 254 (Ark. 1993).

[11] Section 541 of the Bankruptcy Code creates the bankruptcy estate, which consists of all the property that will be subject to the jurisdiction of the bankruptcy court. *See* 5 COLLIER ON BANKRUPTCY ¶ 541.01, at 541-7. Section 541(c)(2) excludes from the bankruptcy estate property of the debtor that is subject to a restriction transfer enforceable under "applicable non-bankruptcy law." *See Patterson*, 504 U.S. at 755. Although some courts have held that IRAs that meet the requirements of § 541(c)(2) are completely excluded from the estate, that issue is not before the Court. *See* 4 COLLIER ON BANKRUPTCY ¶ 522.09[10][b], at 522-64; *see, e.g., Yuhas*, 104 F.3d at 614.

the only IRAs that would qualify for the exemption in § 522 are IRAs that would not be part of the bankruptcy estate at all. *See* 11 U.S.C. § 541. The plain language of § 522(d)(10)(E)(iii) leaves no doubt that IRAs are subject to the exemption.[12] The Eighth Circuit's approach is not just contrary to the text, but illogical. *See Ron Pair*, 489 U.S. at 241; *see also Dubroff*, 119 F.3d at 76.

In addition, the Eighth Circuit's suggestion that retirement contracts or plans might qualify for the exemption if access to them were limited by more than "modest early withdrawal tax penalties," Pet. App. at 6a, lacks support both in fact and in law. Contrary to the lower courts' assumption, a 10 percent penalty is an effective deterrent to early withdrawal. In 1987, for example, nearly $6.5 million dollars had been deposited in IRAs in the nation's credit unions. Yet, that year, only 1.2 percent of that total was withdrawn early enough to trigger a penalty, only 1.27 percent in 1988. *See In re Cilek*, 115 B.R. 974, 988 n.15 (Bankr. W.D. Wis. 1990). Even if some basis existed in fact to distinguish between the deterrent value of different penalty levels, the text of the statute does not support such distinctions. If an IRA complies with the requirements of § 408 and provides that "the right to receive payments" is triggered by one or more of the events listed in § 522(d)(10)(E), it qualifies for the exemption.

The decision on appeal has consequences far beyond its application to IRAs. The ability to withdraw funds prior to reaching 59½ years of age is characteristic of IRAs

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[12] The amount of the exemption remains limited, of course, by the "reasonably necessary" standard.

generally, but it is commonly found in at least some of the four types of plans specifically listed in subsection (d)(10)(E). *See* I.R.C. §§ 401, 403, 72(q), (t).[13] Section 522 authorizes an exemption for "[t]he debtor's *right to receive*" "a *payment* under a stock bonus, pension, profitsharing, annuity, or similar plan or contract *on account of* illness, disability, death, age, or length of service . . . ." 11 U.S.C. § 522(d)(10)(E) (emphasis added). The qualifying phrase "on account of" means that the debtor's right to receive a payment from one of the five sources must be attributable to illness, disability, death, age, or length of service. *See Bank of America*, 526 U.S. at 450 (noting that the common understanding of "on account of" in § 522(d)(10)(E) and other provisions in the code means "because of"). The grammatical structure of the sentence makes the qualifier applicable equally to each of the five possible sources of payments, not only to IRAs and "similar" plans. Limiting the exemption to plans or contracts that permit payments based only on the listed triggering events would drastically curtail the scope of the exemption and destroy the core purpose of § 522(d)(10)(E): protecting "benefits akin to future earnings."

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[13] Those plans or contracts that do permit withdrawals prior to age 59½ generally include vesting requirements that impose additional penalties for premature withdrawals. After an individual's interest has vested, however, withdrawals are subject only to the same 10 percent early withdrawal penalty that affects IRAs.

D. The IRA Exemption Is Indispensable For Older Americans With Less Time To Re-Establish Self-Sufficiency After Bankruptcy.

The number of Americans age 50 and older who are filing for bankruptcy is growing rapidly. The rate of increase in filings is greatest among Americans age 65 and older. *See generally* Teresa A. Sullivan, Deborah Thorne & Elizabeth Warren, *Young, Old, and In Between: Who Files for Bankruptcy?* Norton Bankr. L. Advisor, 1, 8, Sept. 2001; *see* Suein Hwang, *New Group Swells Bankruptcy Court: The Middle-Aged*, Wall Street Journal, Aug. 6, 2004, at 1A. By contrast, younger bankruptcy filers tend to have accumulated too much debt while starting jobs and families, leaving them without enough savings to carry them through lean times. Older Americans generally file for bankruptcy after struggling with one or more crises that upset their financial planning. For them, the modest savings in an IRA can mean the difference between relying on Social Security alone and having some modest additional means to help them cope with the many financial pressures of aging.

A need to provide financial assistance to a family member or to stay home to care for one, a job layoff or forced retirement, or a health related crises such as catastrophic illness or work-related disabilities – all precipitate bankruptcy filings by older Americans. Because the personal savings rate for older Americans, like Americans in general, has continued to decline, these "financial transitions" can be far-reaching enough that the lives of those experiencing them may never be the same. Sophie M. Korczyk, *How Americans Save*, at 1, 28-32, 39 (July 1998), at http://research.aarp.org/econ/9806_save.html; *see also* Verma and Lichtenstein, *The Declining Personal*

Savings Rate: Is There Cause for Alarm?, at 7 (March 2000), at http://research.aarp.org/econ/ib42_alarm.pdf. Even if a person is able to avoid bankruptcy, experiencing one of these crises is a harbinger for vulnerability in retirement. *See* Korczyk at 32.

Consequently, medical problems and the financial stresses of aging often leave Americans, especially those 65 and older, with no choice but to file for bankruptcy. In 2001, at least 20 percent of all Social Security beneficiaries (aged 65 and older) relied on Social Security for 100 percent of their income. Social Security Administration, *Fast Facts & Figures About Social Security*, at 7 (June 2003), at http://www.ssa.gov/policy/docs/chartbooks/fast_facts/2003/ff2003.pdf. Nearly 38 percent of beneficiaries over 65 received 90 percent or more of their income from Social Security. Ke Bin Wu, *Income of Older Americans in 2001: A Chartbook*, at 27 (Aug. 2003), at http://research.aarp.org/econ/ip_cb2001.pdf. The average monthly Social Security benefit for a single retired worker in 2003 was $922 – or 123 percent of the federal poverty guidelines. Although the average monthly benefit in 2003 for a retired worker with an aged spouse was $1,523, the average benefit for a aged widow or widower in 2003 was $888. *See* Social Security Administration, *Legislative Fact Sheet: 2004 Social Security/SSI Information*, (Dec. 31, 2003), at http://www.socialsecurity.gov/legislation/2004_factsheet.doc; *see* 2003 HHS Poverty Guidelines, 68 Fed. Reg. 6456, 6456-58 (Feb. 7, 2003).

Even when an older American has income beyond Social Security benefits, the pressures of deteriorating health and increasing housing-related costs can become overwhelming. In a 2000 study, almost 50 percent of debtors 65 and older

listed a medical reason for the filing, compared with just 7.5 percent of debtors 25 and older. *See* Melissa Jacoby, Teresa Sullivan and Elizabeth Warren, *Medical Problems & Bankruptcy Filings*, Norton Bankr. L. Advisor, 1, May 2000. The pressures of medical costs on older consumers are undeniable. In 2001, health expenditures were the only category where the average expenditure for older consumers exceeded that of all consumers. George Gaberlavage *et al.*, *Beyond 50.04: A Report to the Nation on Consumers in the Marketplace*, at 69 (May 2004), at http://research.aarp.org/consume/beyond_50_cons.html. Expenditures by older consumers on health care accounted for almost $7 of every $10 spent by all consumers for health care in 2001. *Id.*

The daily cost of living increases sharply when retired people are faced with rising costs in other areas. Older consumers, because their homes tend to be older, spend more than average on housing maintenance, repairs, and insurance costs. *Id.* at 66-68. They also spend more than the average for utilities and property taxes. *Id.* Sudden or major repair costs can force them to borrow – and, eventually, leave them no choice but to file for bankruptcy.

For the typical older American emerging from bankruptcy, trying to rebuild savings in their 50s, 60s, or beyond will be difficult at best. Whether they have filed for bankruptcy or not, older workers face special challenges in obtaining employment. When older workers look for a job, it typically takes them longer to find one. *See* Sara E. Rix, *Update on the Older Worker: 2003*, at 2 (June 2004), at http://research.aarp.org/econ/dd97_worker.pdf. Many older Americans become "discouraged workers" – not actively seeking a job because they do not believe work is available, think they lack the necessary background, fear employers

will think them too old, or anticipate some other form of discrimination. *Id.* at 2-3. And discrimination against older Americans in fact continues to be a problem. Rix, *Aging and Work—A View From the United States*, at 14-16 (Feb. 2004), at http://research.aarp.org/econ/2004_02_work.pdf; Rix, *Update 2003*, at 3; U.S. Equal Employment Opportunity Commission, *Age Discrimination in Employment Act (ADEA) Charges, FY 1992-2003*, at http://www.eeoc.gov/stats/adea.html.

If an older American, particularly a displaced worker, is able to obtain a job, it is likely to be a lower paying one at a significant wage loss. *See* Rix, *Update 2003*, at 2-3; Rix, *Aging and Work*, at 10, 17-18. Moreover, basic living expenses often consume their wages, leaving very little, if anything for savings. For those older Americans unable to work because of failing health, caretaker responsibilities or other limitations, the future is likely to be particularly bleak. For them, an exempt IRA will allow them some modest additional means to cope with the many financial pressures of aging.

II. THE EXEMPTION IN § 522(d)(10)(E) FOR IRAs INCLUDES A DEBTOR'S RIGHT TO RECEIVE FUTURE PAYMENTS FROM A QUALIFIED IRA.

In the Third Circuit, courts limit the availability of the exemption in § 522(d) to debtors receiving, or eligible to receive, payments in accordance with the age, illness, disability, or death provisions of I.R.C. §§ 408, 72(t). In other words, a debtor with an IRA in the Third Circuit qualifies for the exemption only if he or she has reached the age of 59½. *See In re Clark*, 711 F.2d 21 (3rd Cir. 1983); *see*

also In re Velis, 949 F.2d 78 (3rd Cir. 1991). *Clark* involved payments from a different type of retirement plan, Keoghs.[14] Although *Velis* did not directly rule on whether *Clark* applies to IRAs, bankruptcy courts in the Third Circuit continue to take the position that the exemption is available only to IRA holders who have reached the age of 59½. *See, e.g., In re Fulton*, 240 B.R. 854 (Bankr. W.D. Pa. 1999).

The Third Circuit's statutory interpretation is inconsistent with both the text and purpose of § 522(d)(10)(E). Yet, if this Court does not conclude that all IRAs qualify for § 522's exemption, it should at least affirm the Third Circuit's approach.

Once again, the language of the statute does not support the age-based distinction imposed by the Third Circuit. Nothing in § 522(d)(10)(E) limits the scope of the exemption to persons who have reached the age of 59½. To qualify for the exemption, the statute's language does not require ongoing payments from the IRA at the time of the bankruptcy petition or even present rights to receive such payments. The statute uses the term "right to receive . . . a payment," a phrase that necessarily encompasses both present and future rights. Nothing in the language chosen by Congress suggests that this right is limited to present payments. By contrast, the application of § 522(d)(10)(E) to both present and future payments is consistent with Congress' express purpose in enacting the exemption: to permit an individual debtor to take out of the estate property necessary to sustain herself, including "certain benefits that

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[14] The Fifth Circuit has characterized the *Clark* decision as "obsolete." *Carmichael*, 100 F.3d at 380.

are akin to future earnings of the debtor." H. Rep. No. 95-595, at 362, *reprinted in* 1978 U.S.C.C.A.N. at 6318.

IRAs are an important part – for some, an essential part – of preparation for retirement. The challenges faced by older Americans in a bankruptcy proceeding are substantial. Depriving persons under the age of 59½ of their IRAs is simply not consistent with Congress' concern for the retirement needs of self-employed individuals, individuals without employer-based retirement plans, and individuals who have rolled pension or other plans into an IRA. A 58-year old person is not significantly better able to recover from the loss of an IRA than a 59½-year old with a present right to payment under an IRA.[15] Both the plain language of the statute and Congress' clearly expressed intent dictate that both present and future rights to payment under an IRA should be eligible for the exemption in § 522(d)(10)(E).

CONCLUSION

For the foregoing reasons, AARP joins the Rouseys in asking this Court to reverse the decision of the U.S. Court of Appeals for the Eighth Circuit and, if the Court is unable to do that, affirm the interpretation in use in the U.S. Court of Appeals for the Third Circuit.

Respectfully submitted,

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[15] Of course, If the circumstances of an individual debtor – whether the debtor is 58 or 65 – indicate that the IRA is not needed for future support, § 522(d)(10)(E) authorizes the trustee to limit the exemption only to amounts "reasonably necessary" for the future support of the debtor and any dependents.

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